Finast

FIRST NATIONAL STORES INC.

ANNUAL REPORT

FOR THE YEAR ENDED
MARCH 29
1969

FINANCIAL HIGHLIGHTS

	52 weeks ended March 29, 1969	*53 weeks ended March 30, 1968*
Sales	$692,125,000	$640,116,000
Income (loss) before income taxes and extraordinary credit	1,619,000	(11,294,000)*
Income (loss) before extraordinary credit	999,000	(6,644,000)
Net income (loss)	1,239,000	(6,644,000)
Per share of common stock:		
Income (loss) before extraordinary credit	.62	(4.14)
Extraordinary credit	.15	—
Net income (loss)	.77	(4.14)
Net working capital	35,118,000	34,910,000
Total assets	128,934,000	123,068,000
Stockholders' equity	85,545,000	84,707,000
Book value per share	53.29	52.77
Number of stores	444	481

*Restated — See note 4 to financial statements.

DIRECTORS

*Hilliard J. Coan
Maurice T. Freeman
John E. Lawrence
John F. Lebor
John L. MacNeil
Edward A. Merkle
*Adrian O'Keeffe
Bernard M. O'Keeffe
*William A. Ryan

*Member of Executive Committee

OFFICERS

Adrian O'Keeffe, *Chairman of the Board*
Hilliard J. Coan, *President*
Alan L. Haberman, *Executive Vice President*
John W. MacNeil, *Vice President*
Richard M. O'Keeffe, *Vice President*
William R. Powers, II, *Vice President*
Peter C. Quinn, *Vice President*
William A. Ryan, *Vice President, Secretary and Clerk*
William A. Ferrara, *Treasurer*
Robert B. McCann, *Controller*

TRANSFER AGENTS

The First National Bank of Boston, Boston, Mass.
Chemical Bank, New York, N.Y.

REGISTRARS

State Street Bank and Trust Co., Boston, Mass.
Bankers Trust Co., New York, N.Y.

TO OUR SHAREHOLDERS:

Somerville, Massachusetts, May 29, 1969

Your management is pleased to report that results for the fiscal year ended March 29, 1969, were greatly improved over those of fiscal 1968. We believe they provide tangible evidence that the programs and policies started in 1967 are restoring Finast to profitable operations and growth.

Financial Summary

Sales in the 52-week fiscal year ended March 29, 1969, increased 8.1 per cent to \$692,125,000 from \$640,116,000 in the 53 weeks of fiscal 1968. Significantly, the gain was achieved by improved volume in identical stores and despite the substantial reduction in total stores.

Sales in the prior year were distorted by two factors which were reported to you in last year's annual report. One was a strike which adversely affected sales in the amount of about \$20 million; the other was a 53-week fiscal year which occurs every sixth or seventh year and increased sales by approximately \$12 million.

Net income for fiscal 1969 amounted to \$1,239,000, equal to 77 cents per share, as compared with a net loss last year of \$6,644,000, or \$4.14 per share. This year's net income was after a tax loss carryforward credit of \$240,000, while last year's net loss was after a tax loss carryback credit of \$5,130,000. Gains on disposal of fixed assets included in net income for fiscal 1969 amounted to \$894,000 compared with \$196,000 in 1968. This year's amount includes approximately \$800,000 of gain resulting from the sales of two properties which were reported in the second and third quarter interim statements.

Fiscal 1969 results include a pretax charge of approximately \$670,000, arising from the LIFO method of inventory valuation. This compares with a pretax charge of \$119,000 in fiscal 1968. The charge for 1969 is substantially greater than those in recent years and is directly related to the rising wholesale cost of products which our industry has been experiencing. The LIFO method of inventory valuation has been used by the Company since 1942. Although LIFO has the effect of reducing income in inflationary periods, it also has the beneficial effect of providing income tax savings.

Net working capital at March 29, 1969, was \$35,118,000 as against \$34,910,000 at the close of fiscal 1968. Current assets at March 29, 1969, amounted to \$75,046,000 and current liabilities were \$39,928,000, or a ratio of 1.88 to 1 compared with a 2.10 to 1 ratio a year earlier.

Net capital expenditures for the year totaled \$5,306,000 up from \$5,140,000 in fiscal 1968. Long-term debt on March 29, 1969, was \$3,461,000 versus \$3,995,000 on March 30, 1968.

Shareholders' equity at the end of the fiscal year was \$53.29 per share, compared with \$52.77 at the close of fiscal 1968.

Dividends

Because of the Company's strong financial position and the continuing improvement in operations, the Directors voted on March 18, 1969, a dividend of 25 cents per share which was paid April 28, 1969. This was the first dividend which we have paid since October 1967. On May 13, 1969, the Directors declared a dividend of 25 cents per share payable July 1 to stockholders of record June 2.

Operational Review

Approximately two and one-half years ago, management was assigned the task of evaluating operational practices, merchandising concepts and organizational structure for the purpose of making the changes necessary to revitalize our business.

The following are highlights of our achievements in these areas.

• Changes in organizational structure instituted in 1967 are in full effect in all our stores and in all our divisions.

• We have moved toward a greater degree of centralization in such vital areas as buying, warehousing, transportation, purchasing and production. At the same time, we have decentralized to give authority to division and local management people, so they may respond directly to the needs of every community and neighborhood in which we operate. This includes reacting to destructive price competition, introducing many ethnic and specialized lines of merchandise and services, and initiating promotional work needed in each area.

• Our internal reporting system is being continually revised to provide more complete information for control and decision-making, including widened applications of our computer installations to various facets of operations.

• Our preoccupation — indeed fussiness — with details that make up the high quality and service of Finast stores inspired us to label our meat counters — where customers are most particular — "Fussy Meat Departments". Consistent high quality of products and fine standards of operations have produced impressive results.

• Private label merchandise is under continuous review to capitalize fully on the established customer acceptance of Finast brands. A major label redesign effort was completed this year. Illustrated on the inside back cover are some Finast products bearing the new labels.

• Product quality continues to be a key to consumer acceptance. Quality control of products sold in our stores is a precise and demanding function. Finast was one of the first in its industry to maintain a laboratory to ensure value and quality for our customers. Our modern, fully-equipped facility tests and measures products of our own manufacture, as well as merchandise produced by others.

• As a step toward expanding our in-store customer services, we opened our first Finast Pharmacy department in December 1968 in our Yonkers, N.Y., store at the Cross County Shopping Center. We anticipate that more pharmacy-prescription departments will be established.

Finast Stores

At the end of the fiscal year, 444 stores were in operation compared with 481 at the same time last year. During the past year, four new stores were opened. All were replacements for previously existing stores. There were 12 major remodelings. Forty-one stores were closed.

There are 12 new stores now under construction and we expect to open a minimum of 15 within the current fiscal year. In addition, we have programmed 16 major remodelings.

Related Diversification

The number one priority for management remains the solid establishment of our supermarket operations. However, we are exploring avenues through which our specialized physical, financial and human potentials can be profitably employed in areas related to our basic business.

As a first step toward entering the institutional food supply business, we formed a subsidiary, One-Stop Institutional Foods, Inc. On April 24, 1969, our Company entered into an agreement to acquire the Suffolk Grocery Co., of Boston, an institutional supplier with an excellent reputation for integrity and service in the New England area. Current sales of Suffolk are approximately $7.5 million per year.

Finast People

The substantial progress which your Company has achieved in the past year could not have been possible without the loyalty, energy and enthusiasm of our 16,000 Finast people. Indicative of the constructive relationship Finast enjoys with its people, more than 1700 were honored this year at seven Service Award dinners.

Incentive programs for store managers and supervisory personnel, started in the second quarter of last year, have had a beneficial effect upon operations and morale. Recently, a committee was formed to make recommendations with respect to establishing an incentive program for executives.

Training programs are being updated and expanded. To improve the effectiveness of these programs, we have developed field-oriented personnel managers charged with maximizing communications between people in all operating areas; created a management development department which aids in improving management capabilities; and established an operations training staff which conducts seminars to instruct our people in new methods and systems being introduced.

Outlook

Over a 70 year period, First National Stores Inc. has developed an excellent consumer franchise based on quality, integrity and fair dealing which, though enviable, cannot be taken for granted. Therefore, we are pursuing an aggressive, competitive merchandising and operations program.

Our progress to date on all fronts leads us to be prudently optimistic that with the continuing — and appreciated — support of our customers, employees and stockholders, our long-range objectives will be achieved.

Respectfully submitted,

Adrian O'Keeffe
Chairman of the Board

Hilliard J. Coan
President

ASSETS

	March 29 1969	March 30 1968 (Note 4)
Current assets:		
Cash	$ 10,973,000	$ 8,741,000
Short-term investments, at cost (approximate market)	9,898,000	2,484,000
Accounts receivable, less allowance for doubtful accounts — $187,000 in 1969 and $25,000 in 1968	4,314,000	4,274,000
Refundable federal income taxes	—	4,904,000
Inventories, at cost (substantially on the basis of last-in, first-out) or market whichever is lower	43,293,000	41,537,000
Prepaid expenses and other current assets	6,568,000	4,671,000
Total current assets	75,046,000	66,611,000
Fixed assets, at cost:		
Land	7,773,000	8,174,000
Buildings owned	31,583,000	32,635,000
Store fixtures, leasehold improvements, machinery and equipment	87,812,000	83,955,000
Automotive equipment	7,767,000	7,389,000
	134,935,000	132,153,000
Less — Depreciation and amortization (Notes 1 and 4)	84,135,000	80,529,000
	50,800,000	51,624,000
Other assets and deferred charges	3,088,000	4,833,000
	$128,934,000	$123,068,000

L STORES INC.

BALANCE SHEET

LIABILITIES

	March 29 1969	March 30 1968 (Note 4)
Current liabilities:		
Accounts payable	$ 25,024,000	$ 21,930,000
Accrued expenses	14,236,000	9,504,000
Current portion of long-term debt	267,000	267,000
Dividend payable	401,000	—
Total current liabilities	39,928,000	31,701,000
4.70% Notes, due in equal semiannual instalments to 1976	3,461,000	3,995,000
Reserve for estimated losses on closed stores (reclassified in 1969 to accrued expenses)	—	2,665,000
Stockholders' equity:		
Common stock, without par value (Note 2):		
Authorized — 2,000,000 shares		
Issued — 1,655,268 shares	31,977,000	31,977,000
Retained earnings (Note 2)	55,385,000	54,547,000
	87,362,000	86,524,000
Less — Treasury stock, at cost, 50,064 shares	1,817,000	1,817,000
	85,545,000	84,707,000
Lease commitments (Note 3)		
	$128,934,000	$123,068,000

FIRST NATIONAL STORES INC.

CONSOLIDATED STATEMENT OF INCOME AND RETAINED EARNINGS

	52 Weeks Ended March 29, 1969	53 Weeks Ended March 30, 1968
		(Note 4)
Sales	$692,125,000	$640,116,000
Gain on disposal of fixed assets — net	894,000	196,000
Other income	715,000	498,000
	693,734,000	640,810,000
Costs and expenses:		
Cost of sales, warehousing, transportation and store occupancy expenses	574,825,000	545,296,000
Direct selling, advertising, general and administrative expenses	110,040,000	98,795,000
Depreciation and amortization (Notes 1 and 4)	7,027,000	7,634,000
Interest expense	223,000	379,000
	692,115,000	652,104,000
Income (loss) before federal income taxes and extraordinary credit	1,619,000	(11,294,000)
Federal income taxes (Note 4):		
Charge in lieu of federal income taxes	(620,000)	(480,000)
Provision for refund of federal income taxes	—	5,130,000
	(620,000)	4,650,000
Income (loss) before extraordinary credit	999,000	(6,644,000)
Extraordinary credit — elimination of charge in lieu of federal income taxes arising from carryforward of prior year net operating loss (Note 4)	240,000	—
Net income (loss)	1,239,000	(6,644,000)
Retained earnings at beginning of year	54,547,000	61,993,000
Cash dividends declared — $.25 per share in 1969; $.50 in 1968	(401,000)	(802,000)
Retained earnings at end of year	$ 55,385,000	$ 54,547,000
Per share of common stock:		
Income (loss) before extraordinary credit	$.62	($4.14)
Extraordinary credit	.15	—
Net income (loss) per share	$.77	($4.14)

CONSOLIDATED STATEMENT OF SOURCE AND USE OF FUNDS
YEAR ENDED MARCH 29, 1969

Source of funds:	
Net income	$1,239,000
Depreciation and amortization	7,027,000
Charge in lieu of taxes relating to prior years depreciation charges (Note 4)	380,000
	8,646,000
Use of funds:	
Net additions to fixed assets	5,306,000
Cash dividends declared	401,000
Reduction in long-term debt	534,000
Reserve for estimated losses on closed stores, reclassified to accrued expenses after charges of $652,000	2,665,000
Other, net	(468,000)
	8,438,000
Increase in working capital	$ 208,000

FIRST NATIONAL STORES INC.

NOTES TO FINANCIAL STATEMENTS

NOTE 1 — Depreciation and Amortization Policies

For financial statement purposes, depreciation and amortization are computed under the straight-line method for assets acquired subsequent to March 26, 1966 and primarily under the sum-of-the-years digits method for previous acquisitions. Estimated useful lives are as follows:

Buildings owned	20-50 years
Store fixtures, leasehold improvements, machinery and equipment	8-25 years
Automotive equipment	3-8 years

NOTE 2 — Common Stock and Retained Earnings

As of March 30, 1968 options to purchase 27,800 shares of the Company's common stock were held by certain officers and key employees of the Company. During the year options for 38,250 shares were issued and options for 4,700 shares terminated. At March 29, 1969 options for 61,350 shares were outstanding at prices ranging from \$27.125 to \$64.25 per share, of which options for 19,550 shares were then exercisable. The options become exercisable in equal annual instalments over a four-year period beginning one year after the date granted. Under the terms of the plan, as amended, additional options for 13,650 shares may be granted at prices no less than the fair market value of the common stock at the date of grant and such options expire not more than five years after the date granted.

At March 29, 1969 the portion of retained earnings available for the payment of cash dividends and acquisition of the Company's common stock was approximately \$8,750,000 as calculated in accordance with the terms of the loan agreement covering the long-term debt.

NOTE 3 — Lease Commitments

At March 29, 1969 the Company was committed under 406 leases covering stores and other properties. The minimum annual rentals under these leases amount to approximately \$10,700,000 exclusive of real estate taxes and other expenses or additional rentals based on percentage of sales. Of the minimum annual rental commitment, approximately 65% related to leases expiring within 10 years and approximately 97% to leases expiring within 15 years. Leases on certain closed stores have not been included in the above totals.

NOTE 4 — Federal Income Taxes

No federal income tax payments are required for 1969 due to the Company's net operating loss carryforward. The charge in lieu of federal income taxes in the consolidated statement of income is comprised of the following:

	1969	1968
Loss carryforward benefits realized	\$240,000	—
Tax effect of depreciation charged in prior years and now allowable	380,000	480,000
	\$620,000	\$480,000

In accordance with recently revised accounting principles the Company has given recognition to a book-tax timing difference relating to depreciation charged to income in prior years which was not then deductible for income tax purposes. As a result of this change the accumulated depreciation has been increased by the cumulative tax effect of prior years which has been charged to other assets and deferred charges, depreciation charges have been reduced by the amount currently allowable and a charge equivalent to the federal income taxes thereon has been provided. The accounts for 1968 have been restated accordingly. These changes had no effect on net income.

At March 29, 1969 the Company has available as a credit against future taxable income through 1973 a net operating loss carryforward of approximately \$3,300,000, of which approximately \$880,000 relates to book-tax timing differences. The tax benefits relating to these timing differences will be applied to deferred tax accounts when such benefits are realized.

The Company also has at March 29, 1969 unused investment tax credits amounting to approximately \$800,000 expiring at various dates through 1976.

NOTE 5 — Pensions

The Company maintains a trusteed noncontributory pension plan. It has been determined that no contribution to the Company plan will be required for several years as a result of the amortization of actuarial gains resulting from a change in the interest assumption and transfer of employees to various union pension plans plus a portion of the unrealized appreciation in the current fund. Total pension costs charged to earnings representing contributions to union plans was \$2,341,000 in 1969 and \$1,507,000 in 1968.

REPORT OF INDEPENDENT ACCOUNTANTS

To the Board of Directors and Stockholders of First National Stores Inc.

In our opinion, the accompanying consolidated balance sheet, the statement of income and retained earnings and the statement of source and use of funds present fairly the financial position of First National Stores Inc. and its subsidiaries at March 29, 1969 and the results of their operations and the supplementary information on funds for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year. Our examination of these statements was made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

Boston, Massachusetts
May 16, 1969

PRICE WATERHOUSE & CO.

FIRST NATIONAL STORES INC.

TEN-YEAR REVIEW (IN THOUSANDS OF DOLLARS EXCEPT FOR PER SHARE AMOUNTS)

	1969[1]	1968[1]	1967[1]	1966[1]	1965	1964	1963	1962	1961	1960
OPERATIONS										
Sales	$ 692,125	$ 640,116	$ 641,896	$ 684,898	$ 706,670	$ 723,402	$ 746,089	$ 711,304	$ 536,486	$ 525,351
Net income (loss)	1,239[2]	(6,644)	(696)[3]	2,404	6,488[4]	7,103	7,788	8,172	7,859	8,223
Net income (loss) per share	.77[2]	(4.14)	(.43)[3]	1.47	3.93[4]	4.33	4.73	4.98	4.80	5.02
Cash dividends per share	.25	.50	1.50	2.50	2.50	2.50	2.50	2.50	2.50	2.50
FINANCIAL POSITION										
Current assets	75,046	66,611	72,557	65,773	59,985	61,502	65,466	68,802	52,100	44,737
Current liabilities	39,928	31,701	32,044	23,666	25,020	31,604	36,663	46,017	29,997	24,226
Net working capital	35,118	34,910	40,513	42,107	34,965	29,898	28,803	22,785	22,103	20,511
Ratio of current assets to current liabilities	1.88	2.10	2.26	2.78	2.40	1.95	1.79	1.50	1.74	1.85
Fixed assets, net	50,800	51,624	57,833	59,017	62,916	66,259	66,312	68,138	58,061	57,172
Total assets	128,934	123,068	132,017	125,824	129,592	134,907	138,994	145,596	115,040	105,503
Long term debt	3,461	3,995	4,529	6,131	6,665	7,733	9,750	10,250	—	—
Stockholders' equity	85,545	84,707	92,246	96,027	97,907	95,570	92,581	89,329	85,043	81,277
OTHER DATA										
Capital expenditures — net	5,306	5,140	4,626	6,311	7,669	11,341	9,967	20,982	9,767	11,239
Depreciation and amortization	7,027	7,634	8,960	10,468	11,367	11,606	12,354	10,533	9,517	9,411
Shares of common stock outstanding (at end of year)	1,605,204	1,605,204	1,608,604	1,631,404	1,638,904	1,639,204	1,639,598	1,647,670	1,637,154	1,637,154
Number of stores (at end of year)	444	481	517	573	600	601	610	632	516	534

[1]Consolidated; parent company only shown for prior years.
[2]Includes extraordinary credit of $240 equal to $.15 per share.
[3]Includes extraordinary credit of $280 equal to $.17 per share.
[4]Includes extraordinary credit of $888 equal to $.54 per share.

A major label redesign effort was completed this year. Illustrated here are some Finast products bearing the new labels.